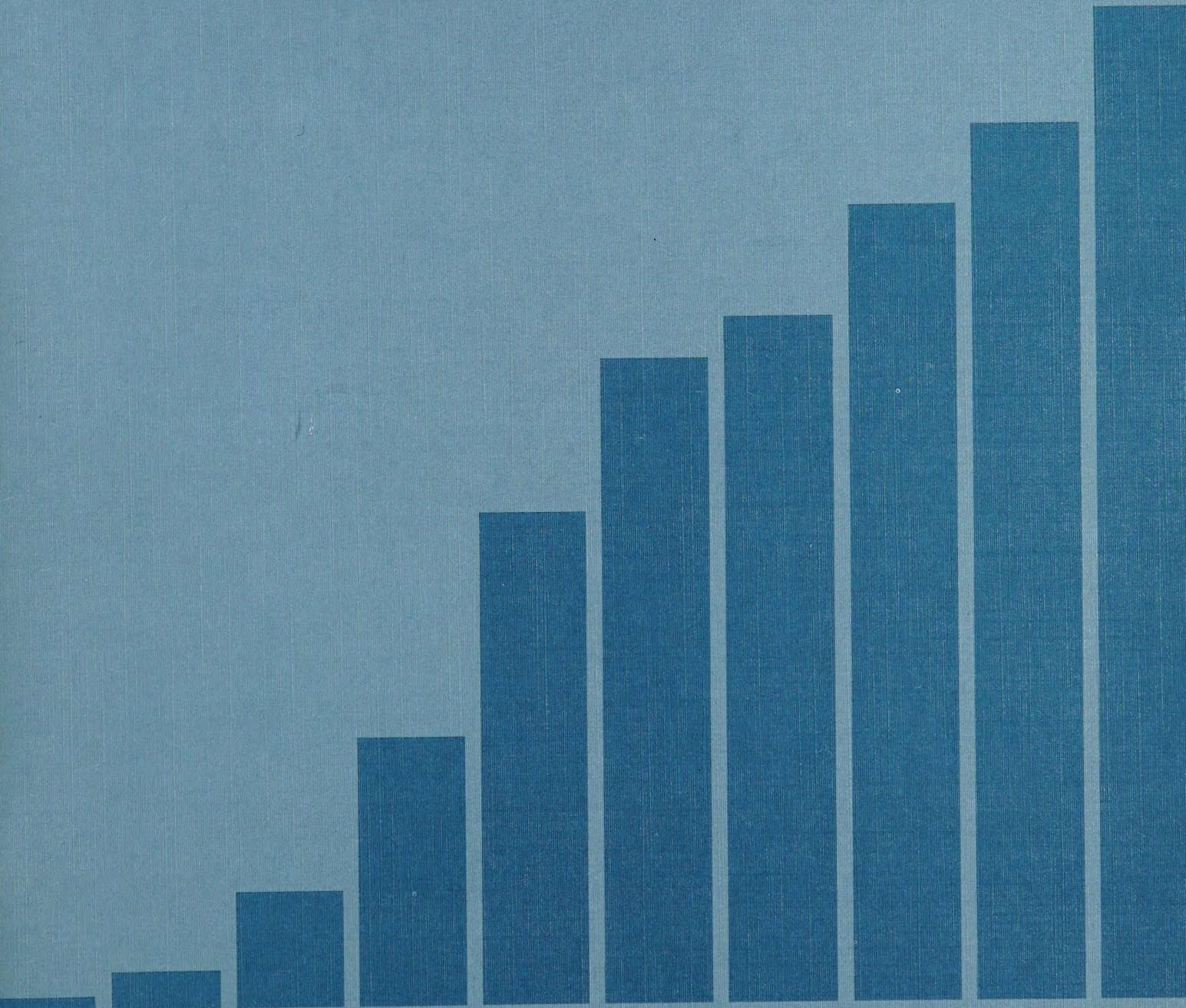


AR50



MERLAND EXPLORATIONS LIMITED



ANNUAL REPORT 1979

THE COMPANY

Merland Explorations Limited is an active independent Canadian public company engaged in the exploration for, development and production of petroleum and natural gas in Canada and the United States. The Company's management and employees, totalling 105, strive to continue the success and rapid growth of Merland in its search for hydrocarbon resources in North America. Our corporate philosophy of well balanced but aggressive exploration, development and acquisition programs assures the Company continued growth potential in the future.

CONTENTS

Highlights	1
President's Report	2
Operations	5
Reserves	9
Exploration	11
Land Holdings	15
Financial Review	21
Financial Statements	23
Five Year Review	31
Corporate Information	Inside back cover

ANNUAL MEETING

The Annual Meeting of the Shareholders of the Company will be held on Tuesday, May 27, 1980 at 9:30 am (MST) in the Main Ballroom at the Holiday Inn, Downtown, Calgary, Alberta, Canada.

HIGHLIGHTS

1. Gross revenue of \$24,002,399 increased 28% over 1978 while net earnings of \$4,855,492 or 80.5 cents per share increased 17%; cash flow from operations of \$11,589,444 or \$1.92 per share increased 38%. Capital expenditures for the year increased 135% over the previous year to a record \$39,105,118.
2. Natural gas production increased 11% to 13.5 BCF or 37.0 MMCFD and crude oil production increased 72% to 158,437 Bbls. or 434 BOPD.
3. Proven and probable natural gas reserves increased 22% to 365 BCF and crude oil reserves increased 45% to 1,440,000 Bbls.
4. Land holdings at the end of 1979 were 1,271,712 gross acres and 473,738 net acres.
5. Merland participated in a total of 282 wells during the year with a success ratio of 82%.

	1979	1978	Percent Change
Financial			
Gross revenue (\$000)	\$ 24,002	\$18,727	+ 28%
Net earnings (\$000)	4,855	4,149	+ 17%
Per Share	0.81	0.70	+ 16%
Cash flow (\$000)	11,589	8,394	+ 38%
Per Share	1.92	1.41	+ 36%
Capital expenditures (\$000)	39,105	16,614	+135%
Operating			
Production			
Natural gas			
Billions of cubic feet (BCF)	13.5	12.2	+ 11%
Millions of cubic feet per day (MMCFD)	37.0	33.4	+ 11%
Crude oil			
Barrels (Bbls.)	158,437	92,089	+ 72%
Barrels per day (BOPD)	434	252	+ 72%
Reserves (Proven and Probable)			
Natural gas (BCF)	365	300	+ 22%
Crude Oil (Bbls. in thousands)	1,440	995	+ 45%
Land holdings (acres in thousands)			
Gross	1,272	1,089	+ 17%
Net	474	352	+ 35%
Drilling record			
Gross wells	282	170	+ 66%
Successful wells	230	131	+ 75%

TO THE SHAREHOLDERS:

The year 1979 was certainly the year of greatest growth and economic expansion which Merland has experienced in its history. Gas and oil sales increased approximately 28% over 1978 resulting in increases of 38% in cash flow and 17% in net earnings. Although there was still some curtailment of natural gas sales due to market restrictions, the price of natural gas and crude oil in Alberta and the United States moved sharply upward at the end of 1979 and in the early part of 1980. A further advancement of oil and gas prices is expected in 1980.

During 1979, Merland participated in the drilling and/or purchase of a record number of wells in Canada and the United States, and our success ratio remained unusually high. Merland spent \$39,000,000 on capital investment during 1979 with approximately \$30,000,000 being expended for exploratory and development drilling, purchases of land and proven reserves while \$9,000,000 was spent on production equipment and facilities. These drilling and land expenditures resulted in an increase of approximately 22% in gas reserves, and 45% in crude oil reserves. Most of these new oil and gas reserves were put on production by the end of the year indicating that 1980 will see a marked increase in most financial aspects of the Company.

Natural gas production was averaging approximately 65.0 MMCFD at the end of 1979 compared to 46.0 MMCFD at the end of 1978. Approximately 95% of this gas production was located in Canada and 5% in the United States. Oil production at the close of 1979 was averaging approximately 600 BOPD compared to 450 BOPD at the end of 1978. Additionally in 1979, Merland substantially increased its oil and gas land holdings with its net acreage position increasing approximately 35%.

OUTLOOK

By taking the maximum advantage of our existing gas sales contracts, Merland has been able to convert natural gas reserves into cash flow more rapidly and efficiently than is general for the industry. This condition is expected to exist for another four or five years, resulting in continued above-average growth in Merland's activities and assets.

It is expected that Merland's cash flow will grow significantly over the next several years and it is planned to use this cash flow to continue to expand our land holdings, crude oil and natural gas reserves, and production facilities.



Robert K. Dixon, President

To date, most of our activity has been concentrated in the shallow to medium depth areas of Alberta. Although we will continue to be very active in these areas in the near future, it is expected that our exploration efforts in northern Alberta, British Columbia and Saskatchewan will increase.

During 1979, Merland established an office in Denver, Colorado. With this "on-the-spot" contact, we are looking forward to more exploration and development activity in the United States, particularly in the states of Colorado, Wyoming, Montana and North Dakota.

Subject to any major property acquisition opportunities that may arise, capital expenditures for the year 1980 are expected to be approximately \$35,000,000 of which approximately \$4,000,000 will be spent in the United States and \$31,000,000 in Canada.

PERSONNEL

Merland's staff has now increased to a total of 105 employees in the field and head office. The activities carried out by Merland during 1979 put our employees through a very trying test. The President and Directors are very pleased to report to our shareholders that through a well co-ordinated and determined effort, Merland's employees passed the test with flying colours and the Company is now reaping the benefits of these efforts. The extra effort which our employees put forth in order to make 1979 such a successful year is greatly appreciated and we are confident that the same hard work and determination will be exhibited by our employees in 1980 and the following years which will assure Merland's continued growth.

On February 26, 1980, the management of Merland Explorations Limited was restructured and several new appointments were made. I am very pleased to advise Merland's shareholders of the following appointments:

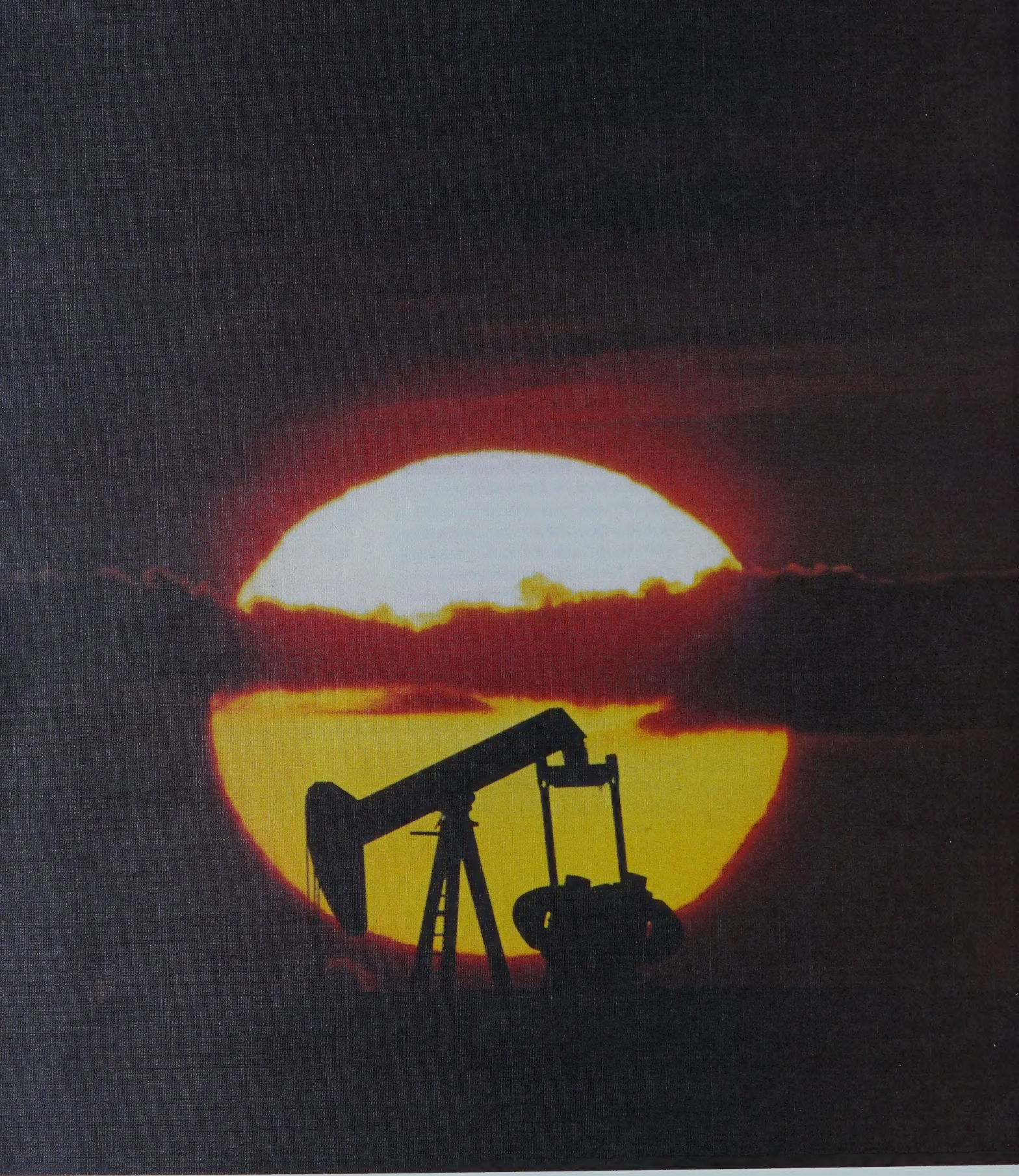
Allan P. Markin
Senior Vice President
Peter W. Kreutzer
Vice President, Finance
and Administration
Douglas A. Weston
Vice President, Exploration
George N. Betts
Vice President, Land and
Joint Interests

I would like to congratulate these gentlemen on their new appointments and I am confident that this restructuring of our management team will result in a continuation of Merland's growth.

On behalf of the Board of Directors

A handwritten signature in dark ink, reading "R. K. Dixon". The signature is fluid and cursive, with the first letters of the first and last names being capitalized and prominent.

President



OPERATIONS



Allan P. Markin
Senior Vice President

Merland Explorations Limited has reached a new plateau in natural gas and crude oil production in 1979 as the total operated natural gas and crude oil sales reached approximately 130.0 MMCFD and 1,400 BOPD at the end of the year. Of these amounts, Merland's share is approximately 65.0 MMCFD and 600 BOPD. During the year 1979, Merland's total net natural gas and crude oil production was 13.5 BCF and 158,437 Barrels which is an increase of 11% and 72% respectively over the year 1978.

The following is a summary of natural gas and crude oil sales from our various projects during the year 1979 as compared to the year 1978:

NATURAL GAS AND CRUDE OIL SALES (NET) BEFORE ROYALTY

PROJECT	1979	1978
Natural Gas (MCF)		
Canada		
Alderson South	38,227	—
Bantry	1,023,557	948,623
Birch Wavy	717,328	407,183
Big Bend North	163,449	139,711
Conlac	3,181,075	4,383,329
Elkwater	220,274	362,983
Halkirk	181,100	275,383
Hilda	531,760	558,371
Holden	200,969	238,027
Horsham	1,022,017	796,205
Jarrow	1,002,559	847,432
Medicine Hat North	901,562	880,882
Vale	2,605,355	1,493,961
Vale South	251,930	18,785
Viking West	156,204	18,258
Westlock	419,387	60,451
Others	31,433	60,451
	<u>12,648,186</u>	<u>11,732,394</u>
United States		
East Texas	749,226	374,823
South Texas	43,136	32,457
Southwest Texas	32,189	30,481
	<u>824,551</u>	<u>437,761</u>
TOTAL GAS (MCF)	<u>13,472,737</u>	<u>12,170,155</u>
Crude Oil & Liquids (Bbls.)		
Canada		
Taber	119,422	67,106
Wimborne	5,310	1,976
Others	664	990
	<u>125,396</u>	<u>70,072</u>
United States		
East Texas	30,488	20,522
South Texas	2,474	1,365
Southwest Texas	79	130
	<u>33,041</u>	<u>22,017</u>
TOTAL OIL & LIQUIDS (Bbls.)	<u>158,437</u>	<u>92,089</u>



At the end of 1979, Merland was operating approximately 20,000 horsepower to compress and process natural gas. During the past year, 7,000 horsepower was added in the various fields on behalf of Merland and its partners at a gross cost of approximately \$6,000,000 and in excess of 160 miles of pipeline were installed at the various projects to gather natural gas at a gross cost of \$6,300,000.

The following is a brief description of the Company's 1979 activities in our major projects:

CANADA

VALE

During the past year, a total of 72 new development and exploration wells were drilled and 2,000

additional compressor horsepower was installed for this project. These additions have resulted in an increase in gross natural gas production to 34.0 MMCFD from 17.0 MMCFD prior to November 1, 1979. Merland's share of this gas production is 20.0 MMCFD. This increase in production is due in part to the discovery of an additional producing horizon in the area which is presently being fully developed.

The Vale Project is now Merland's single largest natural gas producer.

CONLAC

The Conlac Project was producing at a rate of 22.5 MMCFD at the end of 1979 compared to 17.0 MMCFD at the end of 1978.

Merland's share of this production

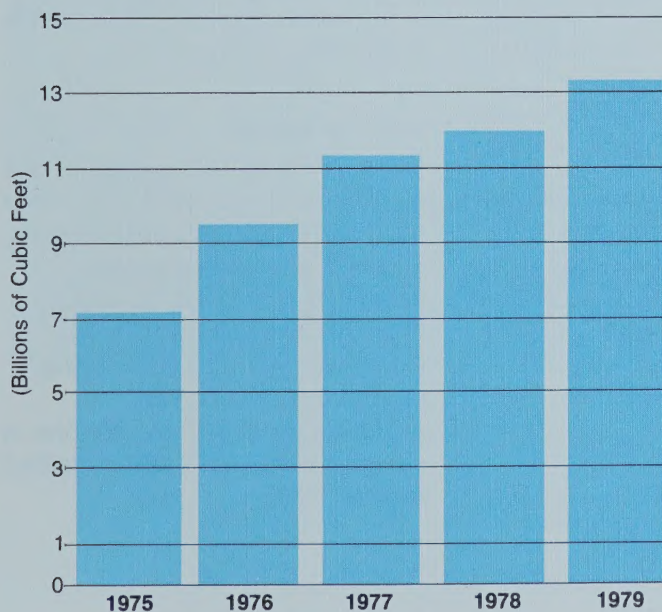
is 10.0 MMCFD. Merland's overall net gas production from the Conlac Project declined during 1979 as payout of Merland's development investment was reached during the year and the Company's working interest was reduced. However, Merland concluded a purchase agreement with other owners in the project whereby Merland's working interest in this project will increase to 100% over the next three years.

A total of 11 wells were drilled on this project during 1979 and a similar number are expected to be drilled during 1980.

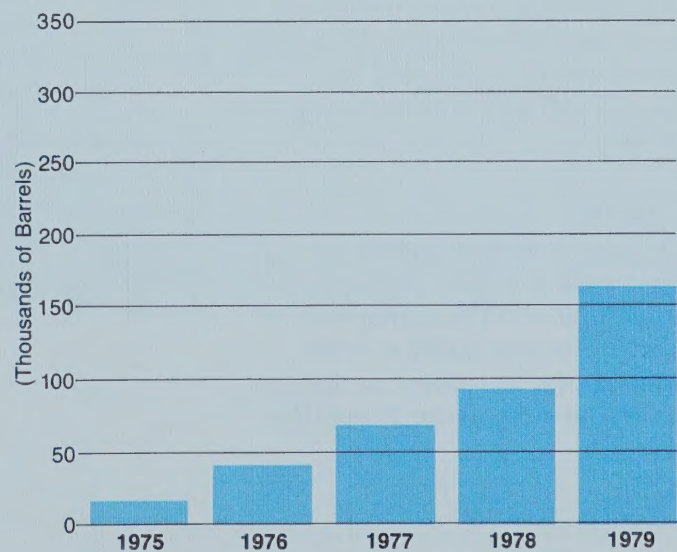
JARROW - BIRCH WAVY

With the passing of time, the Jarrow - Birch Wavy area is becoming more important to

Natural Gas Production



Crude Oil Production



Merland from both an exploration and production point of view. This area contains six separate projects at the present time.

During the year, 86 wells were drilled in this eastern Alberta area, resulting in 57 gas well completions. These new wells resulted in an increase of 150% in proven gas reserves and increased the Company's contracted sales volume in the area to 38 MMCFD, an increase of 200% over 1978. Merland's average share of this production for the year was 17 MMCFD.

Natural gas production from this area is processed through six main compressor stations, some of which are not operating to full capacity at the present time due to restrictions of the gas purchaser's transportation and metering facilities. It is expected that these restrictions will be removed in 1980, resulting in an increase in gas sales.

It is planned that a considerable amount of additional drilling and construction activity will be carried out in this area during 1980.

GIROUX

During 1979, an extensive gas gathering and sales pipeline system, as well as gas compression and processing facilities were installed for this project so that gas sales could commence. Natural gas

and crude oil production from the Giroux Project began on a continuing basis on February 7, 1980, at rates of 2.5 MMCFD and 70 BOPD.

It is possible that one or two additional development wells will be drilled on this project in 1980 if reservoir performance is satisfactory.

STOLBERG

Natural gas production from this deep carbonate reservoir was delayed until the summer of 1980 due to pipeline transmission problems. It is expected that the Stolberg well 10-16-41-14 W5M, Merland's first deep foothills test, will produce at an initial rate of 5 to 7 MMCFD, of which Merland's share is 20%.

TABER

Merland's net crude oil production from the Taber Project in 1979 increased 78% over 1978 as the Company increased its working interest in the project from 17.5% to 32.5% at mid year by purchasing the additional working interest.

A total of 9 wells were drilled on the project in 1979 resulting in 6 successful oil wells and three abandonments. Several additional wells are planned to be drilled during 1980.

UNITED STATES

EAST TEXAS

Natural gas production from Merland's East Texas properties doubled in 1979 and crude oil and natural gas liquids increased 50%.

The No. 1 C. E. Mayes well continues to produce in excess of 10.0 MMCFD of natural gas and 180 BOPD of crude oil and liquids. Merland's share of this production is 20%.

This well has now produced in excess of 4.0 BCF of natural gas and 80,000 barrels of natural gas liquids in one and one half years of production.

The No. 1 and No. 2 C. W. Turner wells also continue to produce at a satisfactory combined rate of 5.0 MMCFD of which Merland's share is 18%.

The Grand Saline crude oil and solution gas project is currently producing approximately 2.5 MMCFD and 600 BOPD of which Merland's share is 7.5%.

SOUTH TEXAS

Several new natural gas reservoirs have been encountered in the deep wells in the Corpus Christie area. These new reservoirs have produced at rates of up to 3.5 MMCFD and 100 BOPD and extensive testing is now being carried out. If reservoir performance is satisfactory one or two additional wells will be drilled during 1980.

RESERVES

GAS AND CRUDE OIL RESERVES

Merland's natural gas, crude oil and natural gas liquids reserves, as of December 31, 1979, have been determined by independent consultants. Merland's total proven and probable natural gas reserves (before royalty) were 365 BCF which represents an increase of 22% over 1978.

The Company's total proven and probable crude oil and liquids reserves (before royalty) were 1,440,000 barrels showing an increase of 45% over 1978.

The area of major increase in reserves was in Alberta with the Jarrow-Birch Wavy and Conlac-Vale areas predominating. The natural gas reserves in Jarrow-Birch Wavy increased 43.0

BCF while gas reserves in Conlac-Vale increased 23.0 BCF. The crude oil reserves increased mainly in the Taber and Giroux Lake areas of Alberta.

The following is a summary of Merland's natural gas, crude oil and natural gas liquids reserves in Canada and the United States as of December 31, 1979.

	Proven		Probable		Total	
	Gas (MMCF)	Oil (Bbls.)	Gas (MMCF)	Oil (Bbls.)	Gas (MMCF)	Oil (Bbls.)
CANADA						
ALBERTA						
Producing	197,712	774,868	36,422	395,574	234,134	1,170,442
Non-Producing	5,224	—	4,901	—	10,125	—
	<u>202,936</u>	<u>774,868</u>	<u>41,323</u>	<u>395,574</u>	<u>244,259</u>	<u>1,170,442</u>
SASKATCHEWAN						
Producing	14,017	—	—	—	14,017	—
Non-Producing	91,820	—	—	—	91,820	—
	<u>105,837</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>105,837</u>	<u>—</u>
BRITISH COLUMBIA						
Non-Producing	3,300	—	—	—	3,300	—
	<u>312,073</u>	<u>—</u>	<u>41,323</u>	<u>—</u>	<u>353,396</u>	<u>—</u>
UNITED STATES						
Producing	11,275	210,277	—	59,534	11,275	269,811
TOTAL	<u>323,348</u>	<u>985,145</u>	<u>41,323</u>	<u>455,108</u>	<u>364,671</u>	<u>1,440,153</u>



EXPLORATION



Douglas A. Weston
Vice President, Exploration

CANADA

In 1979 Merland significantly increased its exploration efforts in the Western Canada Sedimentary Basin. By following the basic philosophy of developing new reserves in traditional gas producing areas and complimenting these reserves with gas and oil projects in the deeper portions of the basin, the Company is building a solid long term gas and oil production base for the future.

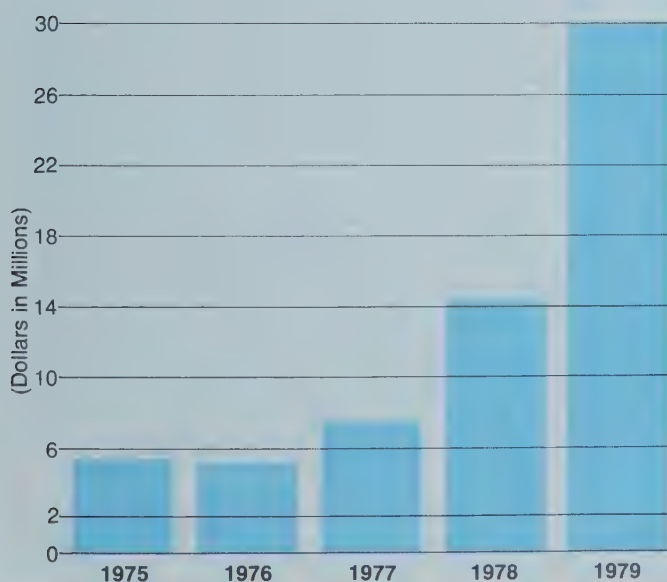
During the past, Merland has consistently increased its capital expenditures and funds directed to the exploration and acquisition of produceable gas and oil properties. The year 1979 represented a record year in the

dedication of funds towards expansion and growth for exploration activities.

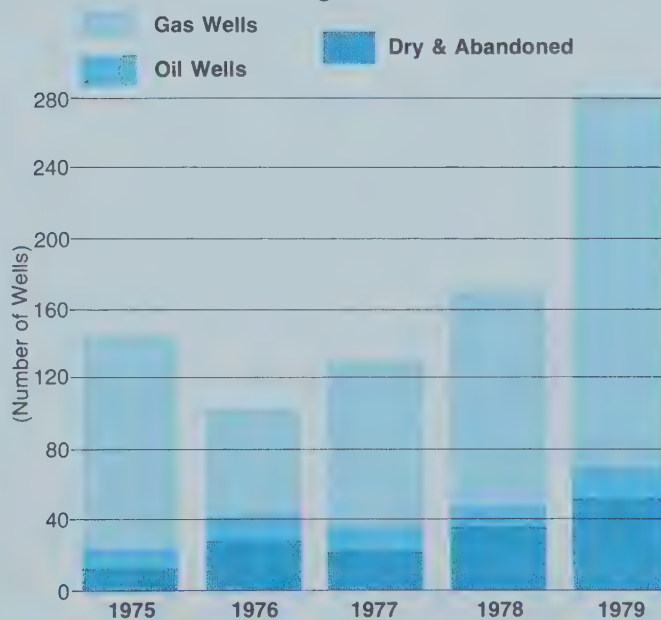
To complement our existing gas producing projects, Merland's exploration efforts were directed to the acquisition of medium depth gas and oil projects and deeper foothills drilling ventures.

Approximately 20% of your Company's 1979 exploratory budget was allocated to these deeper projects. During 1979 Merland drilled or participated in 282 wells in Canada and the United States. Of this total, 230 wells were completed as gas or oil wells for a success rate of 82%.

Land, Drilling & Geophysical Expenditures



Drilling Record



SHALLOW GAS PROPERTIES

Northeast Alberta

Merland participated in the drilling of 22 exploratory wells in the Wandering River and Seibert Lake areas of northeast Alberta in 1979. Sixteen of these wells were cased as gas producers and 6 wells were abandoned. This drilling has significantly extended the field boundaries along this widespread multiple zone producing trend and has increased Merland's gas reserves in this area substantially.

Medicine Hat

Activity continued in our Medicine Hat properties where Merland drilled 84 wells. Improved formation evaluation and completion techniques have greatly increased the producibility and profitability of natural gas reserves from this area. As a result, this area will continue to be a very important exploration region for Merland.

Sand Hills

With the prospect of a new gas sales contract in the Sand Hills area in southwest Saskatchewan, Merland has significantly expanded its proven gas reserve position in Saskatchewan. The development of these proven gas reserves will begin in mid 1980 and will contribute to Merland's natural gas production in the coming year.

MEDIUM DEPTH PROPERTIES

Jarrow-Birch Wavy

The exploration and acquisition of properties in east-central Alberta was again accelerated in 1979. The multi-zone, high deliverability potential that exists within this area in conjunction with an immediate gas market makes the area most economically attractive for Merland. With the conclusion of several farmouts and acquisitions, Merland has increased its acreage holdings and its producible gas reserves in this area. A good portion of the newly acquired acreage is in the heart of the "heavy oil" producing area of eastern Alberta with established producing oil fields such as Wainwright and Viking-Kinsella in very close proximity. Merland has encountered heavy oil reserves in the Sparky, Lloydminster and Colony Sands in several of its natural gas exploration and development wells. There are no plans to develop and produce these heavy oil reserves at the present time, however, further evaluation work will resume once firm pricing and royalty policies are established by the various levels of government.

Northwest Alberta

The northwest sector of Alberta is becoming a very important area to Merland for the establishment of additional oil and gas reserves. As a result, it is expected that a greater percentage of the Company's total exploration funds will be expended in this area in the future.

Several projects with considerable potential were initiated in the Simonette-Karr, Teepee Creek and Worsley areas during 1979. Further seismic, drilling and land acquisition programs are planned for 1980 in these deeper hydrocarbon prone areas.

Northeast British Columbia

During the past year, Merland acquired land holdings in the Redeye, Pickell Creek, Raccoon and Beaton River in the Fort St. John area. Some exploratory drilling was carried out on these projects in 1979 and drilling will resume in early 1980 as part of an ongoing exploration program for the area.

FOOTHILLS

Stolberg

Merland's first "thrust belt" drilling venture resulted in a successful step out well in the Stolberg field. Natural gas production from the Mississippian thrust sheets is expected to commence in 1980 with further development drilling to continue on Merland's acreage during the next year or two.

OIL PROJECTS

Merland participated in the drilling of 17 wells in the Taber, Wimborne and Giroux Lake areas during 1979. Of this total, 11 wells were cased as oil producers and 6 wells were abandoned.

Merland acquired a substantial exploration acreage position in the Dodsland and Shaunavon oil producing areas of Saskatchewan during the year. An aggressive exploration and development drilling program will be carried out in these oil prone areas during 1980.

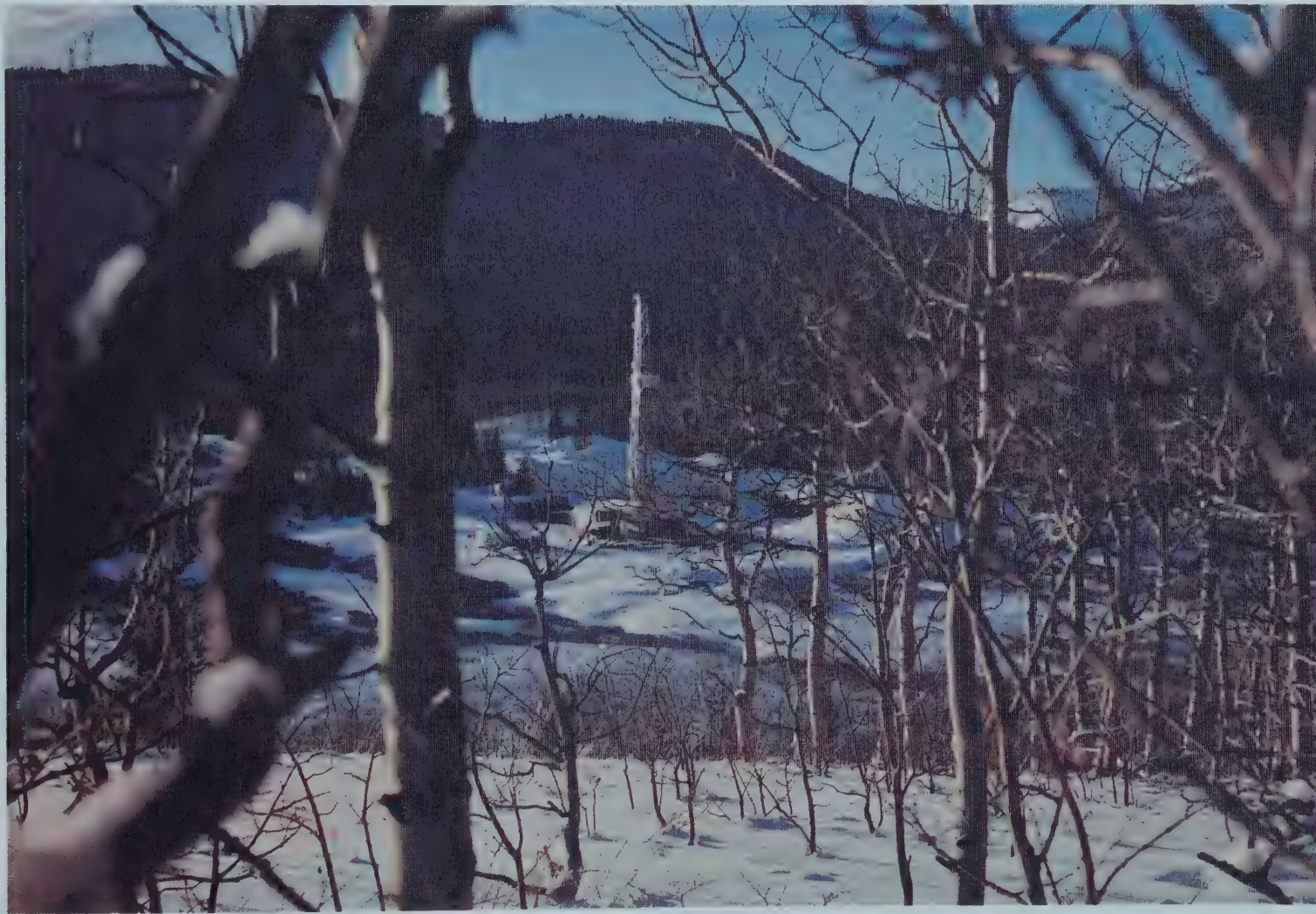
UNITED STATES

An active exploration and development program in the

United States continued in 1979. During the year, the Company participated in the drilling of 20 wells, resulting in 6 gas producers, 5 oil wells and 9 abandonments.

Merland's activities were directed towards the exploration and development of oil and gas projects along the Texas Gulf Coast and in East Texas as well as oil prospects in the Powder River and Williston Basin in the Rocky Mountains. To

compliment Merland's expanding exploratory ventures and long term investment opportunities in the United States, the newly established office in Denver, Colorado, staffed initially with exploration and land personnel, will enhance the Company's activities significantly.





LAND HOLDINGS



George N. Betts
Vice President, Land and Joint Interests

Merland concluded another very successful year in acquiring large blocks of high potential oil and gas properties in Alberta, Saskatchewan and British

Columbia. These acquisitions resulted in a substantial increase in gross and net acres of Merland which reflects our aggressive position in the oil and gas industry and will provide the basis for continued growth of the Company. At the end of 1979, Merland owned a total of 1,271,712 gross acres and 473,738 net acres in Canada and the United States.

ALBERTA

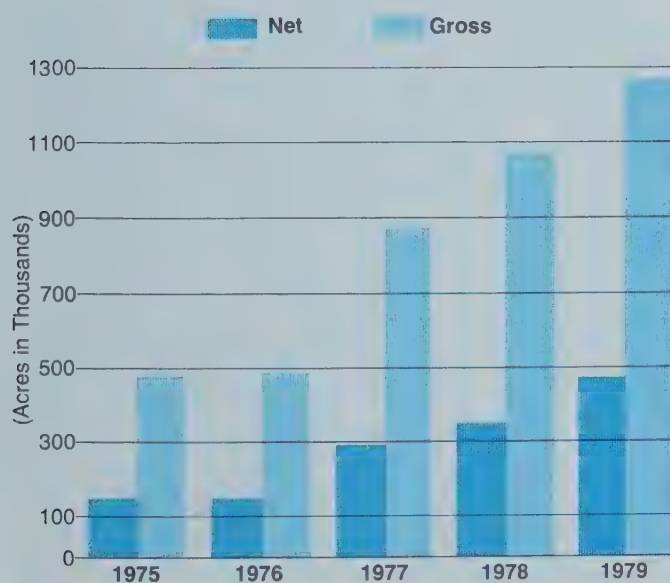
During 1979, Merland acquired 330,795 gross acres and 207,680 net acres in Alberta, resulting in an increase at the end of the year of 43% and 83% respectively over 1978. Particular attention was placed on our Birch Wavy and Medicine Hat areas as these areas provide an immediate increase in cash flow. In the Birch Wavy area, Merland acquired 101,823 gross

acres and 72,712 net acres, resulting in an increase at the end of the year of 70,271 gross and 55,277 net acres over 1978.

Approximately 85% of the newly acquired acreage is proven or semi-proven and a large portion of the proven acreage was drilled during 1979 and placed on production by the end of the year. Merland made two very significant land additions in the Birch Wavy area during 1979 with the acquisition of a 50% working interest in 11,520 gross acres under an agreement for sale and a multi-well farmin on 46,144 gross acres of freehold acreage. This undeveloped acreage gives Merland the opportunity to expand throughout the Birch Wavy area as the land is in several blocks and will allow the Company to pursue a number of geological prospects in the area.

Merland concluded a 20 well earning program in the Medicine Hat area during 1979 which added

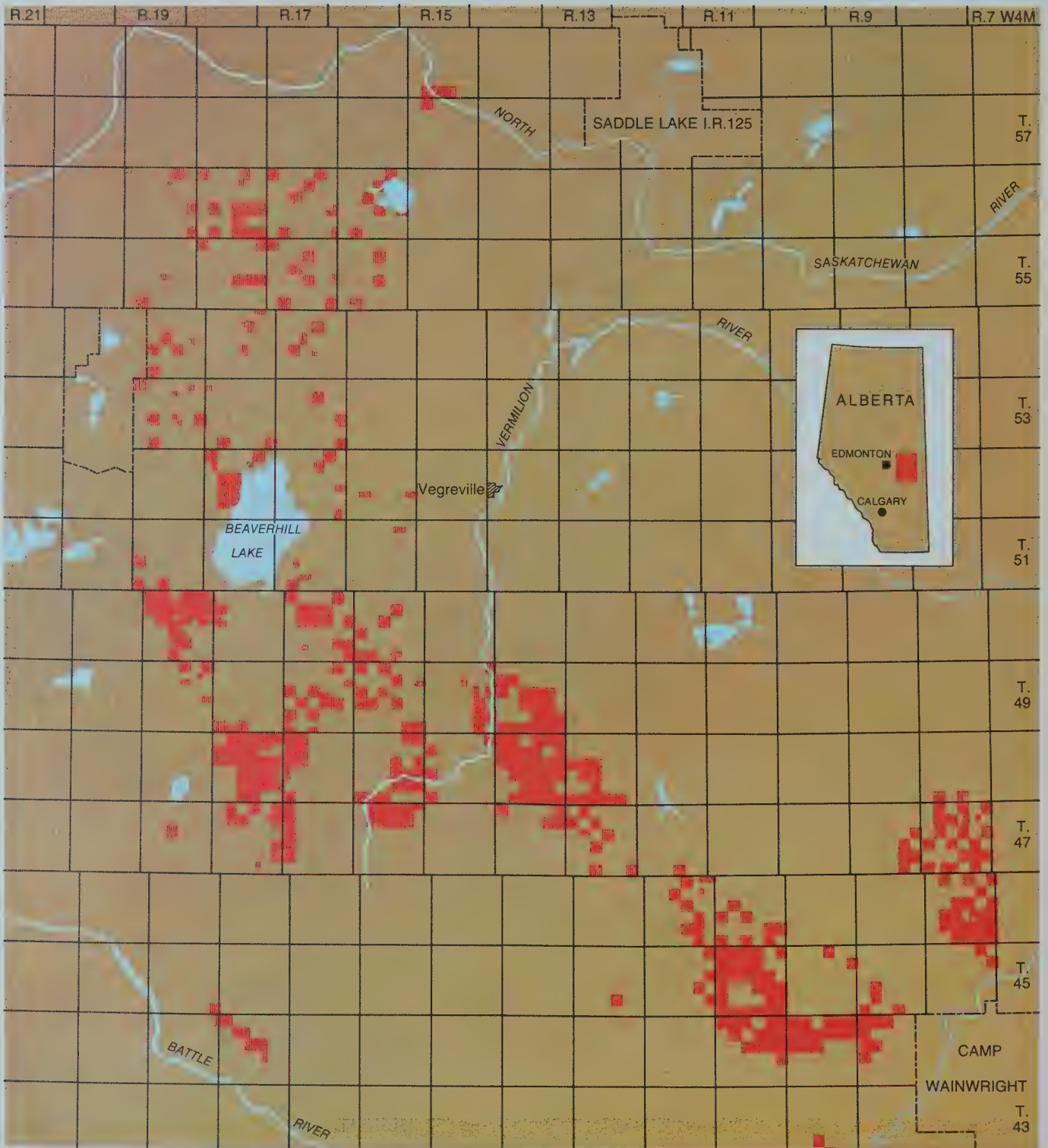
Acreage Holdings



LAND HOLDINGS

	1979 Gross Acres	1979 Net Acres
CANADA		
Alberta	878,077	325,702
Saskatchewan	200,249	111,448
British Columbia ...	48,726	14,636
	<u>1,127,052</u>	<u>451,786</u>
UNITED STATES	<u>144,660</u>	<u>21,952</u>
TOTAL	<u><u>1,271,712</u></u>	<u><u>473,738</u></u>

BIRCH WAVY - JARROW AREA



14,080 gross acres and 6,252 net acres to our contract area. In addition, Merland acquired 4,800 Crown acres in the Medicine Hat area. This acreage was partially developed during 1979 and additional work will be carried out during 1980.

In addition to the above mentioned areas, Merland continued to pursue the expansion of our land holdings in northern Alberta including Giroux Lake, Wandering River, Seibert Lake, Logan River, North Portage and Touchwood. The desire to expand in these areas is a result of the success of our programs previously carried out.

Merland also expanded its acreage position in several other areas in the Province of Alberta, in order to increase the Company's exposure to new geological prospects.

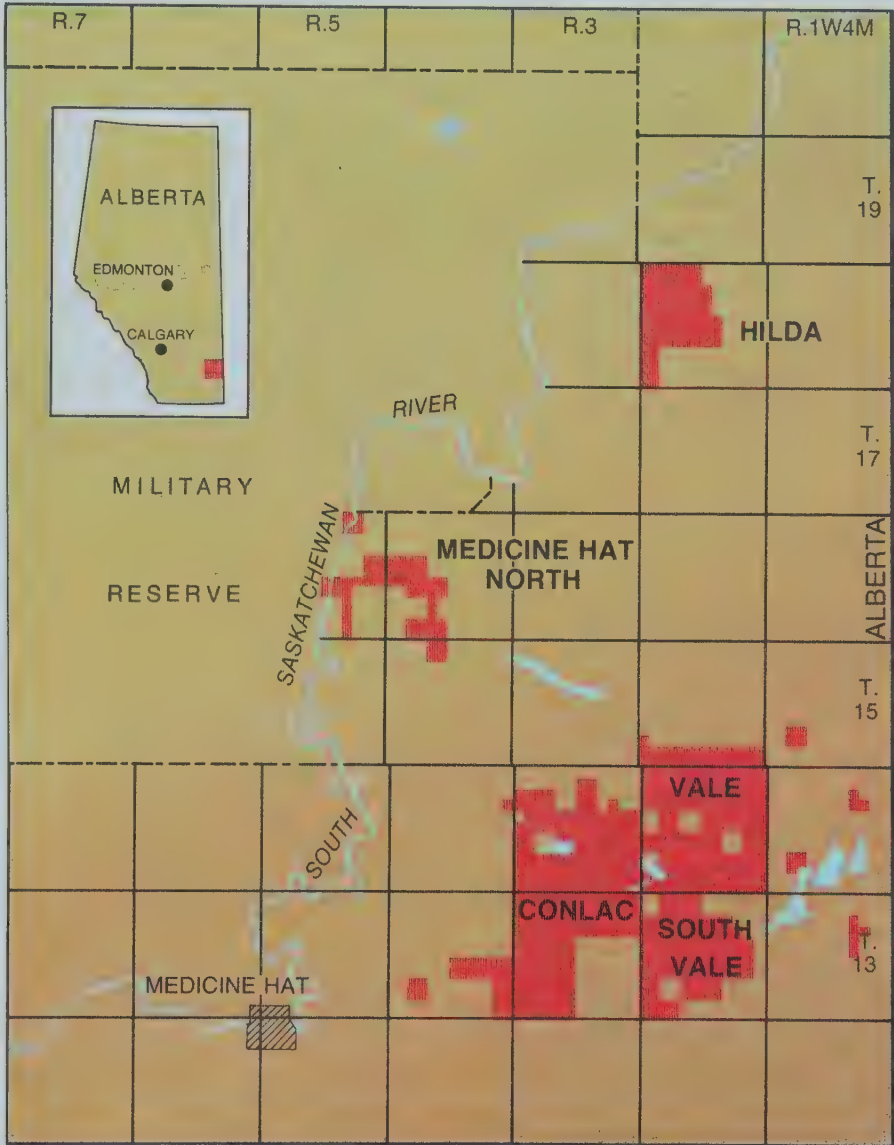
SASKATCHEWAN

During 1979 Merland acquired 128,098 gross acres and 71,307 net acres in the Province of Saskatchewan. Merland now holds 200,249 gross and 111,448 net acres in this Province. These new acquisitions included the purchase of 61,378 acres of freehold lands in the Dodsland area. Merland has high expectations from this Dodsland acreage as it is spread over a large area, portions of which are in close proximity to proven oil and gas reserves. This acreage will provide Merland with a good opportunity to expand its acreage in the area during 1980 as prospects on these lands are developed.

In addition to this acquisition, Merland also expanded its acreage position in the Sand Hills area of southwest Saskatchewan. Merland acquired an undivided 25% working interest in 50,240 gross acres which is an expansion to our existing Sand Hills block. Other

exploration lands have also been acquired in the Success, Rapdan and Antelope areas of southwest Saskatchewan which are close to existing proven oil fields. Merland will pursue exploration programs on these lands during 1980.

MEDICINE HAT AREA



NORTH EAST BRITISH COLUMBIA



BRITISH COLUMBIA

During 1979 Merland acquired 28,803 gross acres and 7,999 net acres in British Columbia increasing our holdings in this Province to 48,726 gross and 14,636 net acres. Land holdings were acquired in the Redeye, Raccoon and Beatton River areas of northeast British Columbia and exploration programs will be carried out on these new prospects during 1980.

British Columbia in general is a relatively new area for Merland and we anticipate participating in several new prospects with the Province during 1980.

The Province of British Columbia has a significant potential for both oil and gas prospects and as a result has recently attracted an increasing number of oil and gas exploration companies. This influx of activity into this area has caused land

prices to escalate to a very high level.

In general, Merland will continue to aggressively acquire additional acreage in the areas mentioned in order that the continued success and growth of Merland will be maintained.

UNITED STATES

Merland concluded an active year in 1979 by participating in new prospects in Montana, North Dakota and Wyoming, together with the continued development of existing prospects in East, South and Southwest Texas.

Merland's land holdings in the United States remained relatively unchanged as to gross and net acres over 1978 as certain leases

were surrendered, while new acreage was acquired in other areas.

Merland holds 144,660 gross acres and 21,952 net acres in the United States as of December 31, 1979.

UNITED STATES





FINANCIAL REVIEW



Peter W. Kreutzer
Vice President, Finance and Administration

Merland continued its financial growth during 1979 with sales, cash flow, earnings and capital investment at record levels. The management is confident that 1980 will once again see record highs in most financial aspects of the Company's operations.

The Board of Directors has recently approved the increase of the authorized capital stock of the Company and a share split on a three for one basis. This will be presented to the shareholders for approval at the annual meeting and if approved will become effective immediately. All figures in this report are presented on a pre-split basis.

REVENUE

Sales from natural gas and crude oil for 1979 totalled \$24,002,399, an increase of \$5,276,000 or 28.1% over the previous year. Increased

production volumes accounted for 49% of the revenue growth and higher selling prices accounted for 51% of this increase.

Net revenue after royalties amounted to \$17,872,044, an increase of 40% over 1978. Total crown and freehold royalties paid were \$6,130,355 in 1979 of which approximately 60% were paid to provincial governments.

EARNINGS

Net earnings for the year 1979 were \$4,855,492 as compared to \$4,148,509 in 1978, representing an increase of 17% and on a per share basis amounted to 80.5 cents per share for 1979 compared to 69.5 cents per share in 1978.

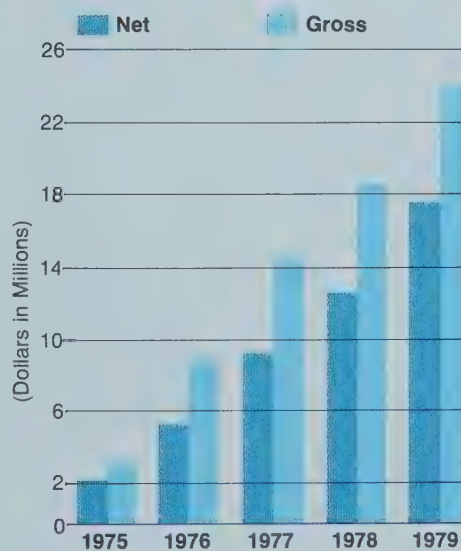
EXPENSES

Crude oil and natural gas production expenses in 1979 increased 47% over 1978, as a

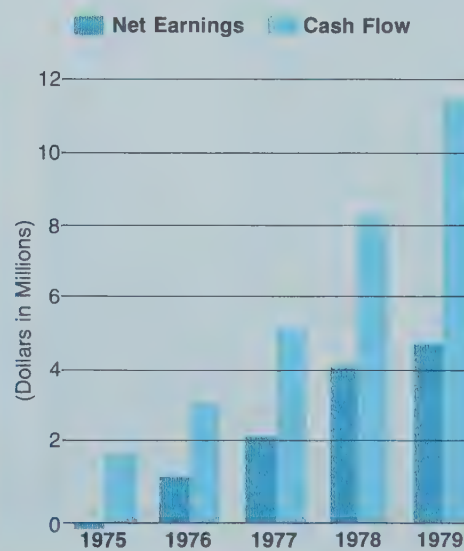
result of the overall increase in natural gas and crude oil production volumes as well as general inflationary trends experienced throughout the industry. The numerous unscheduled shut-downs as a result of cut-backs of natural gas production by major gas purchasers, also adversely affected earnings levels as certain fixed production expenses were still incurred during these shut-down periods. Additionally, the Company undertook substantial maintenance and overhaul programs on production and processing facilities in areas which were shut-in.

Depletion and depreciation have increased over the previous year as a result of the higher cost of acquiring lands, exploring for and developing new petroleum and natural gas reserves.

Gross Sales & Net Sales
After Royalties



Net Earnings & Cash Flow



CHANGES IN FINANCIAL POSITION

Cash flow from operations rose 38% to \$11,589,444 compared to \$8,393,568 in the previous year. On a per share basis, cash flow from operations amounted to \$1.92 for 1979 compared to \$1.41 in 1978.

Under the Company's line of bank credit, \$17,220,000 was borrowed during 1979 to assist in financing the sizeable capital expenditure program. Early in 1980, the Company was able to increase its total bank borrowing capacity to \$90,000,000 which will be secured by the majority of its Canadian petroleum and natural gas properties. This borrowing capacity will provide excellent future financing flexibility.

As a result of gas purchasers not taking delivery of contracted gas, the Company received an amount

of \$1,109,220 in 1979 compared to \$497,994 in 1978 for "take or pay" gas. These amounts have not been reflected in the earnings of the Company. Payments received are considered to be deferred revenue and will not be included in earnings until either the gas is delivered to the purchaser or the period available for the purchaser to take the contracted gas volumes has expired. This "take or pay" represents 4.6% of gross sales compared to 2.6% in 1978.

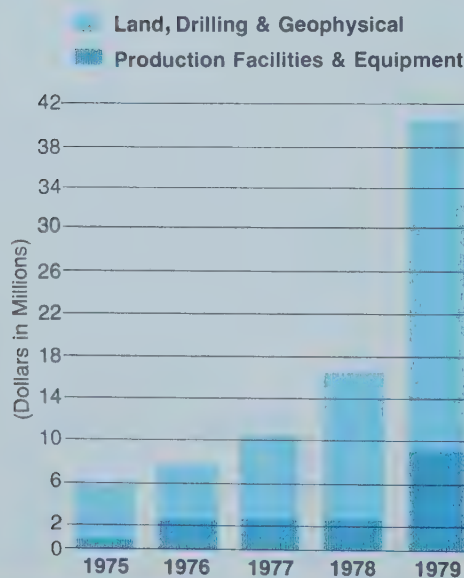
The majority of the capital expenditure program was financed by long-term bank loans, working capital from operations and the sale of certain petroleum and natural gas interests. Approximately 96% of the \$39,105,000 of capital expenditures were made in Canada and 4% in the United States. The major

categories of expenditures were as follows:

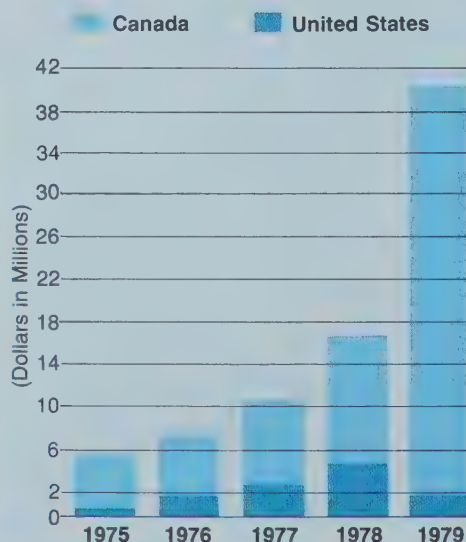
	In thousands
Acquisitions of petroleum and natural gas interests	\$14,838
Drilling and geophysical	15,307
Plants, pipelines and production facilities	8,960
	<u>\$39,105</u>

The successful performance of the Company during 1979 has placed Merland in an excellent position for continued expansion and growth in the oil and gas industry in North America. The present value of its oil and gas reserves and land holdings provides the Company with strong financial capabilities for the future.

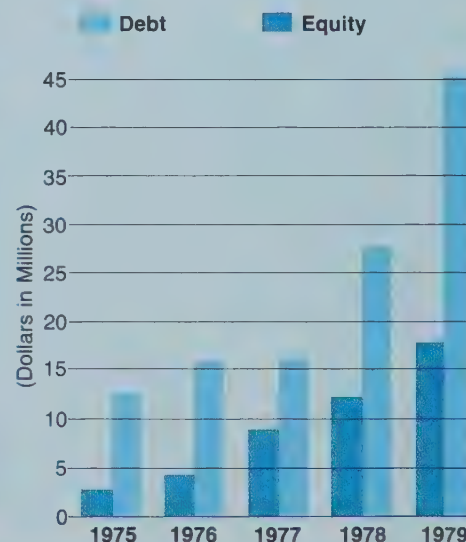
Capital Expenditures



Capital Expenditures



Debt & Equity



MERLAND EXPLORATIONS LIMITED

Consolidated Statement of Earnings

Year Ended December 31, 1979

	1979	1978
REVENUE		
Sales of petroleum and natural gas	\$24,002,399	\$18,726,542
Less royalties	6,130,355	5,982,494
	<u>17,872,044</u>	<u>12,744,048</u>
EXPENSES		
Production	2,755,471	2,322,119
General and administrative	1,244,135	1,185,328
Interest on long-term debt	3,904,361	2,210,241
Depletion	2,516,891	1,434,660
Depreciation	776,410	445,038
	<u>11,197,268</u>	<u>7,597,386</u>
	6,674,776	5,146,662
OTHER INCOME		
Interest	644,601	262,298
Unrealized gain (loss) on foreign currency translation	(15,947)	192,000
	<u>628,654</u>	<u>454,298</u>
EARNINGS BEFORE INCOME TAXES	7,303,430	5,600,960
INCOME TAXES (Note 7)		
Deferred	3,440,651	2,365,361
Alberta royalty tax credit	(992,713)	(912,910)
	<u>2,447,938</u>	<u>1,452,451</u>
NET EARNINGS	<u>\$ 4,855,492</u>	<u>\$ 4,148,509</u>
EARNINGS PER SHARE	<u>80.5¢</u>	<u>69.5¢</u>

MERLAND EXPLORATIONS LIMITED

Consolidated Balance Sheet

December 31, 1979

ASSETS

CURRENT ASSETS

Cash and term deposits	\$ 2,322,298	\$ 6,494,496
Accounts receivable	9,376,644	3,826,858
Promissory note (Note 2)	212,000	—
Pipeline aid in construction loans (Note 3)	102,689	—
Prepaid expenses	57,289	91,717
	<u>12,070,920</u>	<u>10,413,071</u>

PROMISSORY NOTE

— 212,000

PIPELINE AID IN CONSTRUCTION LOANS

— 316,332

PROPERTY, PLANT AND EQUIPMENT (Note 4)

Petroleum and natural gas properties and production equipment	80,979,066	47,217,830
Accumulated depletion and depreciation	<u>9,774,041</u>	<u>6,477,740</u>
	<u>71,205,025</u>	<u>40,740,090</u>

\$83,275,945 \$51,681,493

LIABILITIES

CURRENT LIABILITIES

Accounts payable and accrued liabilities	\$10,654,238	\$ 6,272,573
Current portion of long-term debt	1,722,000	—
	12,376,238	6,272,573

DEFERRED NATURAL GAS REVENUE	1,607,214	497,994
------------------------------------	------------------	---------

LONG-TERM DEBT (Note 5)	43,464,000	27,966,000
-------------------------------	-------------------	------------

DEFERRED INCOME TAXES	8,039,746	4,599,095
-----------------------------	------------------	-----------

SHAREHOLDERS' EQUITY

SHARE CAPITAL (Note 6)

Authorized — 7,500,000 shares without par value	7,238,190	6,650,766
Issued — 6,057,855 (1978 — 5,997,625)	10,550,557	5,695,065

RETAINED EARNINGS	17,788,747	12,345,831
	\$83,275,945	\$51,681,493

On behalf of the Board:

R. K. Rexford, Director

W. L. Matthews, Director

MERLAND EXPLORATIONS LIMITED

Consolidated Statement of Retained Earnings

Year Ended December 31, 1979

	1979	1978
RETAINED EARNINGS AT BEGINNING OF YEAR	\$ 5,695,065	\$ 1,546,556
Net earnings	4,855,492	4,148,509
RETAINED EARNINGS AT END OF YEAR	<u>\$10,550,557</u>	<u>\$ 5,695,065</u>

Consolidated Statement of Changes in Financial Position

Year Ended December 31, 1979

	1979	1978
WORKING CAPITAL DERIVED FROM		
Operations	\$11,589,444	\$ 8,393,568
Sale of income debentures	—	27,966,000
Promissory note	212,000	—
Long-term bank loan	15,498,000	10,130,000
Issue of share capital	587,424	363,028
Sale of property, plant and equipment	5,346,882	2,324,850
Decrease in pipeline aid in construction loans	316,332	50,604
Deferred natural gas revenue	1,109,220	497,994
	<u>34,659,302</u>	<u>49,726,044</u>
WORKING CAPITAL APPLIED TO		
Purchase of property, plant and equipment	39,105,118	16,614,481
Repayment of long-term bank loan	—	24,460,140
	<u>39,105,118</u>	<u>41,074,621</u>
INCREASE (DECREASE) IN WORKING CAPITAL	(4,445,816)	8,651,423
Working capital (deficiency) at beginning of year	4,140,498	(4,510,925)
WORKING CAPITAL (DEFICIENCY) AT END OF YEAR	<u>\$ (305,318)</u>	<u>\$ 4,140,498</u>

Notes to Consolidated Financial Statements

December 31, 1979

1. Significant accounting policies

a) Principles of consolidation

The consolidated financial statements include the accounts of the Company and its subsidiaries, all of which are wholly-owned.

b) Property, plant and equipment

The Company follows the full cost method of accounting for petroleum and natural gas properties and related expenditures, under which all costs related to the exploration and development of petroleum and natural gas reserves are capitalized recognizing separate Canadian and United States cost centres. Such costs include those related to lease acquisitions, geological and geophysical activities, carrying charges of non-producing properties, drilling of productive and non-productive wells and overhead related to exploration and development.

Depletion of petroleum and natural gas properties and depreciation of production equipment are calculated on the unit-of-production method based upon estimated proven reserves as determined by independent engineers. Other equipment is depreciated at rates of 10% to 30% calculated on a declining balance basis.

c) Foreign currency translation

The foreign currency accounts of the Company and its United States subsidiary are translated to Canadian dollars as follows:

Current assets and current liabilities at the rate of exchange prevailing at the end of the year;

Other assets and liabilities at the rate of exchange in effect on the dates the assets were acquired or the obligations were incurred;

Revenue and expenses at the average rate of exchange in effect during the year with the exception of depletion and depreciation, which reflect the rate in effect when the related assets were acquired.

All gains and losses arising from foreign currency translation are included in the determination of net earnings.

d) Joint interest operations

Substantially all of the Company's petroleum and natural gas exploration and production activities are conducted jointly with others and accordingly these financial statements reflect only the Company's proportionate interest in such activities.

2. Promissory note

The promissory note, which is non-interest bearing, represents funds advanced by a subsidiary to an officer and director for the purpose of acquiring shares of Merland Explorations Limited.

MERLAND EXPLORATIONS LIMITED

3. Pipeline aid in construction loans

These loans represent the Company's share of prepaid pipeline construction costs under natural gas sales contracts. The loans are being repaid at fixed rates based on natural gas throughput.

4. Property, plant and equipment

	December 31, 1979			1978
	Cost	Accumulated Depletion and Depreciation	Net Book Value	Net Book Value
Canada				
Petroleum and natural gas properties	\$50,244,313	\$5,702,904	\$44,541,409	\$23,238,232
Production equipment, gas plants and other equipment	19,605,177	2,524,559	17,080,618	8,812,010
	<u>69,849,490</u>	<u>8,227,463</u>	<u>61,622,027</u>	<u>32,050,242</u>
United States				
Petroleum and natural gas properties	9,751,085	1,346,286	8,404,799	7,518,047
Production equipment, gas plants and facilities	1,378,491	200,292	1,178,199	1,171,801
	<u>11,129,576</u>	<u>1,546,578</u>	<u>9,582,998</u>	<u>8,689,848</u>
Total	<u>\$80,979,066</u>	<u>\$9,774,041</u>	<u>\$71,205,025</u>	<u>\$40,740,090</u>

5. Long-term debt

The long-term debt is comprised as follows:

	1979	1978
Bank loans	\$17,220,000	\$ —
Current portion	(1,722,000)	—
	<u>15,498,000</u>	<u>—</u>
Income debentures		
Canadian	20,000,000	20,000,000
United States (\$7,000,000 U.S.)	7,966,000	7,966,000
	<u>27,966,000</u>	<u>27,966,000</u>
	<u>\$43,464,000</u>	<u>\$27,966,000</u>

The bank loans bear interest at the bank's prime lending rate plus $\frac{3}{4}\%$ and are due on demand with terms of repayment over 10 years.

The income debentures have a final maturity date of June, 1988, with quarterly principal repayments commencing September, 1983. Principal repayments by year are as follows:

<u>Year</u>	<u>Canadian Dollars</u>	<u>United States Dollars</u>
1983	\$ 1,500,000	\$ 525,000
1984	3,000,000	1,050,000
1985	3,500,000	1,225,000
1986	4,500,000	1,575,000
1987	5,000,000	1,750,000
1988	2,500,000	875,000
	<u>\$20,000,000</u>	<u>\$7,000,000</u>

The income debentures bear interest at one half of the bank's prime lending rates, plus 1³/₈% until July 1983, and plus 1¹/₈% from August 1983 to maturity.

Certain of the Company's Canadian producing petroleum and natural gas properties are pledged as security for the bank loans and the income debentures.

6. Share capital

During the year, the following shares were issued for cash:

	<u>1979</u>		<u>1978</u>	
	<u>Number</u>	<u>Value</u>	<u>Number</u>	<u>Value</u>
To trustee of deferred profit sharing plan	9,914	\$105,462	10,843	\$ 59,635
Under employee share purchase plan	21,816	333,527	29,505	226,518
Upon exercise of share options	28,500	148,435	22,500	76,875
	<u>60,230</u>	<u>\$587,424</u>	<u>62,848</u>	<u>\$363,028</u>

At December 31, 1979 options granted to officers and employees to purchase shares of the Company were outstanding as follows:

<u>Expiry date</u>	<u>Number</u>	<u>Option price</u>
August 7, 1981	16,000	\$ 5.50
September 27, 1981	15,000	\$ 9.56
March 12, 1983	10,000	\$13.725
	<u>41,000</u>	

The exercise of these options would have no dilutive effect on earnings per share.

MERLAND EXPLORATIONS LIMITED

7. Income taxes

The provision for income taxes differs from the result which would be obtained by applying the combined Canadian Federal and Provincial income tax rate of 47% to the earnings before income taxes. This difference results from the following items:

	1979	1978
Computed expected tax	<u>\$3,432,612</u>	<u>\$2,632,451</u>
Increase (decrease) in taxes resulting from:		
Royalties and other payments to provincial governments	1,946,684	1,977,887
Provincial rebate	(5,723)	(116,055)
Alberta royalty tax credit	(992,713)	(912,910)
Federal resource allowance	(1,922,232)	(1,482,013)
Tax depletion on Canadian production income	(1,030,237)	(852,138)
Non-deductible interest on income debentures	1,039,338	381,209
Other	(19,791)	(175,980)
Income taxes	<u>\$2,447,938</u>	<u>\$1,452,451</u>
Percentage of earnings before income taxes	<u>33.5%</u>	<u>25.9%</u>

8. Statutory information

During the year, the Company had ten directors and four officers, two of whom were also directors. Aggregate remuneration paid to officers for their services was \$246,455 (1978 — \$171,590, four officers) and to directors for their services was \$93,800 (1978 — \$72,100, ten directors).

Auditors' Report to the Shareholders

We have examined the consolidated balance sheet of Merland Explorations Limited as at December 31, 1979 and the consolidated statements of earnings, retained earnings and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the company as at December 31, 1979 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Calgary, Canada
February 25, 1980

Paul, Manu, Mitchell & Co.
Chartered Accountants

FIVE YEAR REVIEW

FINANCIAL (Dollars in thousands except per share amounts)

	1979	1978	1977	1976	1975
Gross sales before royalties	\$24,002	\$18,727	\$14,467	\$9,148	\$3,660
Sales net of royalties	17,872	12,744	9,383	5,698	2,594
Net earnings (loss)	4,855	4,194	2,016	1,128	(53)
Per Share	0.81	0.70	0.34	0.22	(0.01)
Cash flow	11,589	8,394	5,469	3,106	1,850
Per Share	1.92	1.41	0.93	0.62	0.40
Capital expenditures	39,105	16,614	10,341	7,699	5,914
Long-term debt	45,186	27,966	16,615	16,384	12,500
Shareholders equity	17,788	12,345	8,942	4,557	2,662

OPERATING

Production

Natural Gas

Billions of cubic feet	13.5	12.2	11.5	9.6	7.3
Millions of cubic feet per day	37.0	33.4	31.6	26.3	20.1

Crude Oil

Barrels	158,437	92,089	64,556	42,172	15,770
Barrels per day	434	252	177	116	43

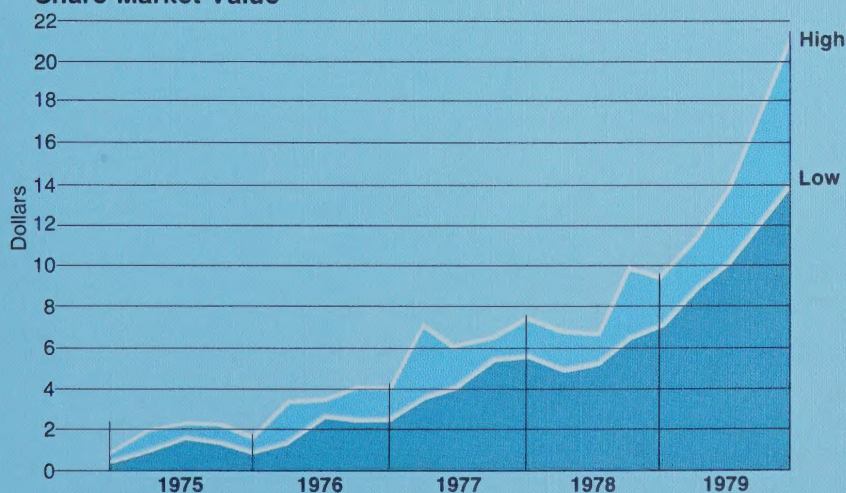
Land Holdings (in thousands of acres)

Gross	1,272	1,090	886	493	487
Net	474	352	297	162	165

Drilling Record

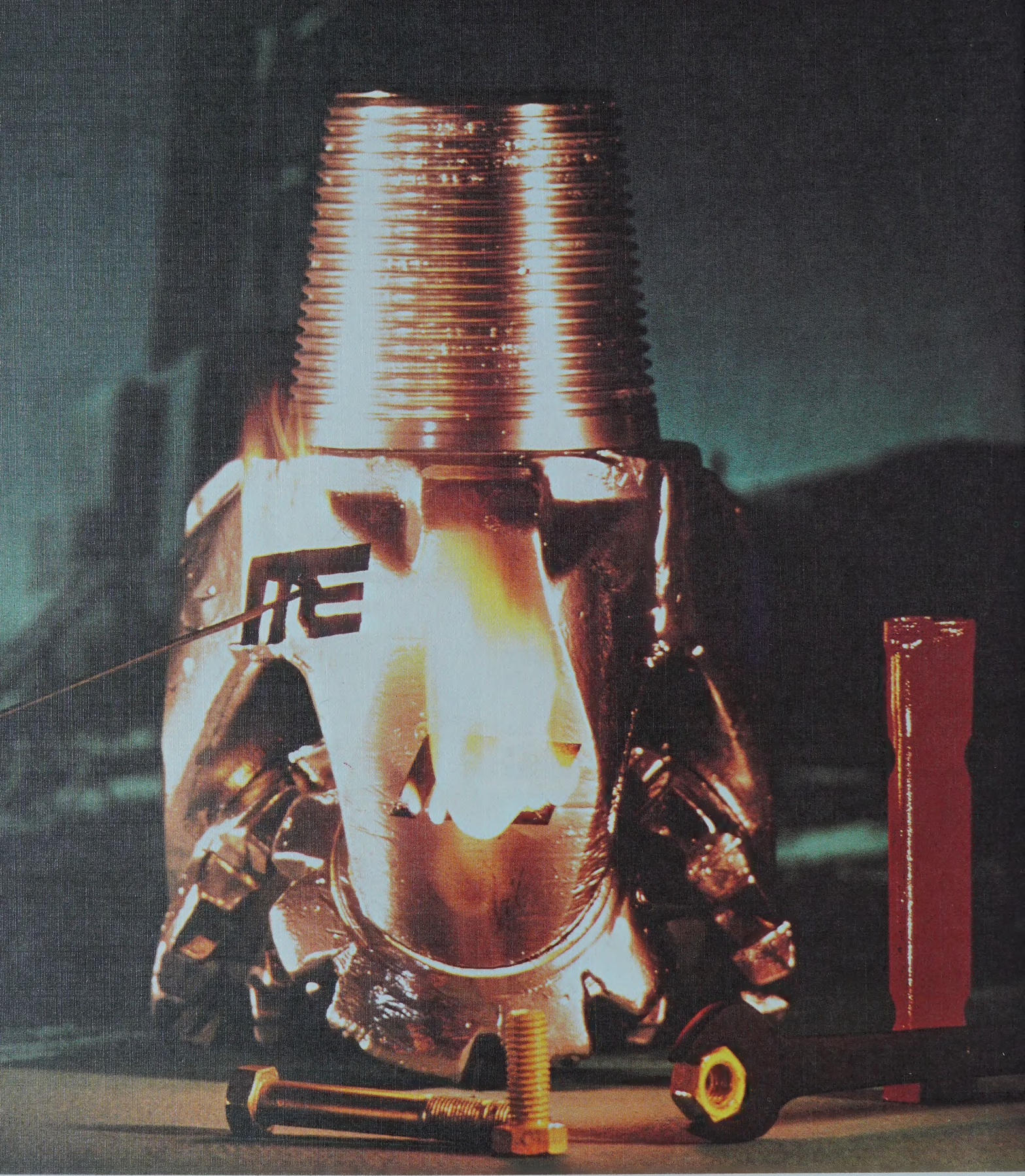
Gross wells	282	170	133	103	145
Successful wells	230	131	112	75	132
Success ratio	82%	77%	84%	73%	91%

Share Market Value



NUMBER OF SHARES TRADED

1975	996,690
1976	3,625,724
1977	4,928,583
1978	5,049,885
1979	6,309,075



CORPORATE INFORMATION

DIRECTORS

Walter J. Adams, Calgary, Alberta
President, Compass Investments of Alberta Limited

Robert K. Dixon, Calgary, Alberta
President, Merland Explorations Limited

George E. Gathercole, Mississauga, Ontario
President, George E. Gathercole Consultants Inc.

Robert Law, Q.C., Toronto, Ontario
Partner, Blackwell, Law, Spratt, Armstrong & Grass
(Barristers & Solicitors)

Brian D. Marshall, Toronto, Ontario
President and Director, RoyMark Financial
Services Limited

Wilmot L. Matthews, Toronto, Ontario
Director, Burns Fry Limited

William O. Parlee, Q.C., Edmonton, Alberta
Partner, Parlee, Irving, Mustard & Rodney
(Barristers & Solicitors)

Harry J. Richardson, Toronto, Ontario
Senior Officer, Tom & Barnt Limited

George T. Smith, Toronto, Ontario
President, Chief Executive Officer,
Northgate Exploration Limited

Donald J. Wilkins, Toronto, Ontario
Chairman, Acklands Limited

OFFICERS

Robert K. Dixon	President
Allan P. Markin	Senior Vice President
Peter W. Kreutzer	Vice President, Finance and Administration
Douglas A. Weston	Vice President, Exploration
George N. Betts	Vice President, Land and Joint Interests
Robert Law, Q.C.	Secretary

SENIOR PERSONNEL

Clayton H. Woitas	Operations Manager
James D. Herbison	Controller
Wayne J. Skinner	Chief Geologist
Robert N. James	Chief Landman

HEAD OFFICE

402, 736 - 8th Avenue, S.W.
Calgary, Alberta
Canada T2P 1H4
Telephone: (403) 269-2511
Telex No.: 03-826866

UNITED STATES OFFICE

2620, 717 - 17th Street
Denver, Colorado
U.S.A. 80202
Telephone: (303) 623-9423

SUBSIDIARY COMPANIES

Merland Resources, Inc.
Merland Oil & Gas, Inc.

AUDITORS

Peat, Marwick, Mitchell & Co.
Calgary, Alberta

BANKERS

The Royal Bank of Canada
Calgary, Alberta

REGISTRAR AND TRANSFER AGENT

Guaranty Trust Company of Canada
Calgary, Alberta
Toronto, Ontario
Vancouver, British Columbia

LISTING

Toronto Stock Exchange
(Symbol MOC)



MERLAND EXPLORATIONS LIMITED

ANNUAL REPORT 1979